



Employees' Retirement Board of Rhode Island
Monthly Meeting Minutes
Wednesday, May 8, 2013
9:00 a.m.
2nd Floor Conference Room, 50 Service Avenue

The Monthly Meeting of the Retirement Board was called to order at 9:04 a.m. Wednesday, May 8, 2013, in the 2nd Floor Conference Room, 50 Service Avenue, Warwick, RI.

I. Roll Call of Members

The following members were present at roll call: General Treasurer Gina M. Raimondo; Vice Chair William B. Finelli; Gary R. Alger, Esq.; Daniel L. Beardsley; Frank R. Benell, Jr.; Roger P. Boudreau; Michael R. Boyce; John P. Maguire; John J. Meehan; Thomas A. Mullaney; Claire M. Newell; Louis M. Prata and Jean Rondeau.

Also in attendance: Frank J. Karpinski, ERSRI Executive Director and Attorney Michael P. Robinson, Board Counsel.

Recognizing a quorum, Treasurer Raimondo called the meeting to order.

Mr. M. Carl Heintzelman arrived at 9:08 a.m., and Mr. Richard A. Licht arrived at 9:10 a.m.

II. Approval of Minutes

On a motion by Frank R. Benell, Jr., and seconded by William B. Finelli, it was unanimously

VOTED: To approve the draft minutes of the April 5, 2013 Special Meeting and the April 10, 2013 meeting of the Employees' Retirement System of Rhode Island.

III. Chairperson's Report

Treasurer Raimondo asked Attorney Gayle Mambro-Martin to update the Board on the disability process. The Treasurer acknowledged Attorney Mambro-Martin's and other staff members' diligence on the work done thus far. Attorney Mambro-Martin said that they modified placement of the disability hot-line number on the ERSRI website to better service the members. She noted that there were 157 calls related to general inquiries such as members own personal retirement status and 4 calls related to members receiving a disability pension where ERSRI needed to further investigate. Attorney Mambro-Martin also noted that disability compliance is on schedule acknowledging Attorney Andrew Marcaccio's efforts. She said of the 517 mailings sent out in January, 155 disability retirees have not yet responded. Currently additional mailings were being made to those members as a follow up. Attorney Mambro-Martin then discussed Independent Medical Examinations (IME). She said ERSRI is working

on securing additional physicians by working with Coastal Medical and Lifespan to retain services thus expediting those members needing assignment to an IME.

Treasurer Raimondo then reported a 9.8% return for the one-year performance and 8.75% for the 3-year performance. She said the standard deviation, which is a measure of risk, is about 12.00%. The Treasurer affirmed that the strategy is to achieve strong long-term returns at lower risk which is being accomplished.

Treasurer Raimondo then introduced Ms. Anne Marie Fink, Chief Investment Officer, to provide an overview of the Fund to the Board. Ms. Fink's discussion began with discussion of an article taken from the April 23, 2013's edition of The Wall Street Journal entitled "*Investors Fault a Model Portfolio For Falling Far Behind the Times*" regarding universal challenges in generating returns given the current low interest rate environment.

Ms. Fink then provided the Board with an update from ERSRI's alternative investment consultant Cliffwater LLC, who presented at the recent State Investment Commission meeting. Cliffwater had shared highlights from the consultancy's recent analysis of the publicly available Comprehensive Annual Financial Reports from 97 state pension plans. Regarding allocations, she told the Board that 90 of the 97 states have some exposure to alternative investments with an average allocation of 24% compared to ERSRI's current allocation of 26%. Ms. Fink then discussed expense ratios; she noted that only 38 of 97 state pension funds reported direct expense information in FY2012. Ms. Fink also said that based on the report from Cliffwater LLC, the average expense ratio is 0.40% and ERSRI's ratio is 0.36% which is modestly below the FY2012 average. Including performance fees, which she noted only five other plans disclose, the ERSRI expense ratio was 0.58% in FY2012 which was at the low end, reflecting only a partial year of hedge fund investments.

During Ms. Fink's presentation were the following questions and answers:

Q: Mr. Maguire asked what is the definition of "opportunistic" under "Data"?

A: Ms. Fink said it is a "catch-all" in that it includes anything other than a traditional bond or equity funds, e.g. timber or pharmaceutical royalties where some universities own the rights to a royalty and they want the money immediately so they will sell off the right to collect on the royalty over time.

Q: Mr. Boudreau asked what percentage of SIC's 26% of alternatives are in the hedge funds?

A: Ms. Fink said 15% of the 26% are in hedge funds.

Q: Mr. Licht asked how Ms. Fink values the alternative investments given that they have no market value?

A: Ms. Fink broke the answer into 2 categories: hedge funds and private equity/real estate. She said hedge funds are easy because they own securities with market values. She said hedge funds own equities, derivatives, and fixed income instruments; they have 3rd party administrators that serve an audit function marking the holdings to market on a monthly basis. She said the SIC picked low risk, low volatility and highly liquid hedge funds that provide diversification, often investing in instruments such as commodities and currency that are not elsewhere in the portfolio. Consequently, if the market were to drop drastically, ERSRI should not experience losses as bad as in 2008. The Treasurer noted that these funds are marked to market daily because they hold liquid securities.

Regarding private equity and real estate, Ms. Fink noted that private equity is difficult to mark to market since private equity does not trade publicly. She said private equity generally marks positions quarterly, based on actual transactions or publicly traded comparables. Discussing real estate, Ms. Fink said appraisals of buildings may sometimes be an estimate of worth based on comparisons to other buildings in its vicinity. She said marks for private equity and real estate have some discretion involved and that is why these funds make incentive fees not off the marked appraisals. Such incentive fees are only earned when the real estate or private companies are sold.

Q: Mr. Licht asked if they buy a building in their fund for \$1 million and sell it for \$2 million, do they have whatever their incentive is, say 20%. He then asked what happens if the opposite occurs, namely, buy it for \$1 million but sell it for \$500,000, what do they get?

A: Ms. Fink said in the first instance yes, the funds earn 20% on the profit and in the second they get nothing.

Q: Mr. Licht then asked, "Are they charged against their other fees and is it a negative incentive?"

A: Ms. Fink said yes, other fees are deducted in the profit calculation and that any losses generally offset gains elsewhere when determining profit.

Q: Mr. Boudreau asked what percentage of fees and expenses are based on the alternative investments?

A: Ms. Fink did not have the numbers but said a large portion is the alternatives due to the deliberate strategy of concentrating fees where ERSRI is likely to get the most value. Alternatives (private equity, hedge funds and real estate), though they are more expensive have more tools at their disposal to generate better returns. For the remainder of the portfolio, the SIC has chosen ultra-inexpensive vehicles, getting its primary exposure to the equity markets via index funds, unlike a traditional portfolio that uses active managers, e.g. mutual funds where one stock is selected over another and that can be costly. Concentrating fees where ERSRI is getting value and then remaining in the minimal-cost index funds is the goal.

Q: Mr. Boudreau asked how do the management fees as a percentage balance against the returns for that portion of the portfolio?

A: Using the graph on page 4, Ms. Fink showed how hedge funds have performed in both risk and reward terms, with reward on the y axis, and risk on the x axis. She noted hedge funds as the low risk component of the portfolio returned less but had a lot less risk. She commented it was a good trade-off.

Q: Mr. Boudreau asked if we did not have the fees, what would the risk be?

A: Ms. Fink said it clearly would be higher. What would be ideal per Ms. Fink is to have all the hedge funds' tools and be inexpensive. However, based on the managers we have found fees are part of the process to access the tools.

Q: Mr. Alger asked when interest rates rise, how does this help us?

A: Ms. Fink said it should help ERSRI a lot since in the traditional 60/40 portfolio, 40% is in bonds. So if interest rate were to rise say to 4% from the current 2%, ERSRI could see a 20-30% drop and she would expect the hedge funds would do fine and avoiding a big downdraft that the 60/40 portfolio would have.

The Treasurer noted that it is incredibly hard to manage money in this market. Since our fund is relatively underfunded, and our job is to make sure peoples' pension is there when needed, the SIC is more worried about the downside than the upside. We could still have a 60/40 portfolio but that would have more risk. Given that and the overall economy, that is not what SIC chose to adopt.

Q: Mr. Licht asked hypothetically if the hedge funds are less risky, then how are the hedge funds' risk measured?

A: Ms. Fink said the "go to" measure for risk in investment business is volatility, i.e. how much an asset goes up and down compared to its long-term average. In 1990, an index for funds was created giving a benchmark of hedge funds. She said the volatility of hedge funds is significantly lower vs. global equities which have volatility as high as 20%. She noted that the volatility of our hedge funds since we invested was 2.6%.

Q: Mr. Boudreau asked the Treasurer about the 1-year return of 9.8%, specifically, where 26% of portfolio is in alternatives and what is the return of the 26% and the other 74% of the portfolio?

A: Ms. Fink noted that the total fund was 11.8% and hedge funds were 8%. Referring to the May 22, 2013 SIC Monthly Meeting report, she said alternatives performance is delineated. She noted that private equity has been up almost 10%; equity hedge funds up 9.7%. Ms. Fink said it has been a really good equity market and SIC has reduced the risk a lot. The real proof will be over the long term and how the SIC's strategy does during up and down markets.

Ms. Fink concluded her presentation with a discussion about risk and return, stating the goal of the SIC is to manage both since lower risk leads to better returns over time. She shared the risk-adjusted return numbers for the last 18 months (since the hedge funds added) for the ERSRI hedge fund allocation, the overall ERSRI portfolio, a benchmark 60% stock / 40% bond asset mix, and global equities. Due to the better risk-adjusted return of the hedge funds, the overall ERSRI portfolio has had a better return and lower risk than the 60% stock / 40% bond mix. Overall, she said the hedge fund portfolio behaved as intended.

Lastly, Ms. Fink discussed the markets for the month of March.

Treasurer Raimondo next asked Attorney Robinson to provide an update on the ethics advisory opinion concerning the ability of certain members to participate in discussions regarding lawsuits against the ERSRI Board. Attorney Robinson told the Board that the Ethics Commission issued the advisory opinion requested by the Board. He noted that they met on April 23, 2013 and advised that 7 members of the Board holding leadership positions in plaintiff organizations must recuse both from participation in discussions and from decision making regarding pending pension reform litigation. The Ethics Commission said those members of the Board, namely Richard A. Licht, Thomas A. Mullaney, and Treasurer Gina M. Raimondo who are named defendants did not need to recuse.

Mr. Prata asked Attorney Robinson why the report was issued on April 15, 2013 and he did not receive a copy of the opinion until the afternoon of April 23. He asked if anyone had received this report prior to his receiving it as a Board member. Attorney Robinson said the Ethics Commission's staff attorney had provided him a draft opinion that the Commission staff considered confidential until the full Ethics Commission considered the matter at the April 23rd meeting, and that the draft opinion was subject to change,

was not a formal advisory opinion of the Commission, and could not be relied upon by the Retirement Board until such time as it had been considered by the full Ethics Commission on April 23.

IV. Executive Director's Report

Director Karpinski apprised the Board that the Procurement Subcommittee meeting was canceled due to a lack of a quorum and will be rescheduled.

He said the Legislative Subcommittee met on April 29, 2013 to discuss an item relating to the SRA Plus benefit option. Richard A. Licht was voted Chairman and Roger P. Boudreau, Vice Chairman. The Director said Mr. Licht would provide updates under the committee reports.

The Director said the Rules and Regulations Subcommittee will be meeting tomorrow morning at 9:30 a.m. and will discussing a regulation on partial leave and an item transmitted by the Legislative Subcommittee.

Director Karpinski noted that he sent an email on May 1, 2013 related to the Board's training session presented by Attorney Robert D. Klausner on March 29, 2013 which related to strategic planning of 9 items. The Director asked that board members offer feedback on meeting times.

Regarding the IT contract, Director Karpinski said ERSRI is still negotiating and narrowing many details. He said he is targeting the June meeting for presentation to the Board.

Director Karpinski apprised the Board that they were in possession of the Pension Application Report, the Disability Subcommittee Report and a 2012 Schedule of Findings and Responses from the Auditor General. Director Karpinski said the Audit Subcommittee will be scheduled to review the report.

Director Karpinski provided a new report of delinquent contributions of both the Municipal Employees' Retirement System of Rhode Island (MERS) and the Employees' Retirement System of Rhode Island (ERS). Director Karpinski discussed how the report is compiled and when an employer is considered delinquent. Mr. Alger asked if there is a penalty for late submission. The Director said there are no provisions in the statute for such a penalty. Board members felt there should be since employee contributions are being withheld. Richard A. Licht and Attorney Dingley said they would discuss the issue and consider legislation.

Lastly, Director Karpinski said the actuarial audit is in process and all the data has been transmitted.

V. Administrative Decisions

Administrative Appeal – Chief David E. Desjarlais vs. ERSRI

Included in Board Members' Books was the Hearing Officer's written decision, along with exhibits and supporting information in the matter of *Chief David E. Desjarlais vs. ERSRI*. Attorney Robinson asked if consistent with Regulation Number 4, *Rules of Practice and Procedure for Hearings*, there were any written briefs, legal memoranda, or exceptions to the decision of the Hearing Officer which must have been submitted to

the Executive Director not later than 10 days prior to the hearing. Director Karpinski apprised the Board that any such material had been included in their board packets.

Attorney Robinson then said that pursuant to ERSRI's regulations, each party to the proceeding has the right to appear and to make oral arguments before the Retirement Board. Consistent with the Board's long standing policy and procedures, he apprised the appellant that this is not an opportunity to present new factual material to the Board, and that pursuant to ERSRI's regulations and Rhode Island case law, the Board owes deference to the Hearing Officer on factual determinations and questions of credibility, and cannot overturn the Hearing Officer on determinations of fact or credibility unless such determinations are found to be clearly wrong.

Attorney Robinson then asked the appellant's Attorney, John J. Lynch, Jr., if Chief Desjarlais would be making any presentation or oral argument before the Board. The appellant was not sworn as Attorney Lynch did not intend to have Chief Desjarlais speak. Attorney Robinson then provided a synopsis of the *Chief David E. Desjarlais vs. ERSRI* matter. There being a stenographer present, the parties presented their cases.

At the conclusion of the hearing, a motion was made by John P. Maguire and seconded by Richard A. Licht to overturn the Hearing Officer's decision and permit Chief Desjarlais to use additional amounts in Final Average Salary (FAS) for computation in his pension. A roll call was taken, and the following members voted Yea: General Treasurer Gina M. Raimondo; Vice Chair William B. Finelli; Gary R. Alger, Esq.; Daniel L. Beardsley; Frank R. Benell, Jr.; Roger P. Boudreau; Michael R. Boyce; M. Carl Heintzelman; Richard A. Licht; John P. Maguire; John J. Meehan; Thomas A. Mullaney; Claire M. Newell; Louis M. Prata and Jean Rondeau.

There being 15 votes cast, 15 voted in the affirmative, consistent with Rhode Island General Laws §36-8-6, *Votes of the Board -- Record of Proceedings*, there being a majority vote of the members present and voting at which a quorum was present, it was then

VOTED: To overturn the Hearing Officer's decision and permit Chief David E. Desjarlais to use additional amounts of Final Average Salary (FAS) for computation of his pension.

VI. Approval of the April Pensions as Presented by ERSRI

On a motion by Roger P. Boudreau and seconded by John P. Maguire, it was unanimously

VOTED: To approve the April pensions as presented.

Mr. Prata left the meeting prior to the Legal Counsel Report.

VII. Legal Counsel Report

Attorney Robinson apprised the Board that a decision came down from Judge Taft-Carter on April 23, 2013, regarding *Anne Melvin vs. ERSRI*. It was an appeal from the Board's denial of an accidental disability application regarding a juvenile program worker at the RI Training School. She was seeking a disability pension due to Post Traumatic Stress Disorder due to multiple instances of harassment at work. Judge Taft-

Carter affirmed the Retirement Board's decision. Attorney Robinson said the member may petition the Rhode Island Supreme Court for a writ of certiorari, and he will keep the Board apprised of any updates.

Consistent with Rhode Island General Laws section §42-46-5 (a) (2) regarding pending or potential litigation involving the Retirement System, a motion was made by Richard A. Licht and seconded by William B. Finelli to convene the Board in Executive Session to discuss each of the 4 bulleted items under the Legal Counsel Report on the agenda and for approval of the sealed executive session minutes from the April 5, 2013 and April 10, 2013 Retirement Board meetings. A roll call vote was taken to enter into Executive Session and for the discussion mentioned above; the following members were present and voted Yea: General Treasurer Gina M. Raimondo; Vice Chair William B. Finelli; Gary R. Alger, Esq.; Daniel L. Beardsley; Frank R. Benell, Jr.; Roger P. Boudreau; Michael R. Boyce; M. Carl Heintzelman; Richard A. Licht; John P. Maguire; John J. Meehan; Thomas A. Mullaney; Claire M. Newell and Jean Rondeau. It was unanimously

VOTED: To convene the Board in Executive Session pursuant to Rhode Island General Laws section §42-46-5 (a)(2) to discuss pending or potential litigation involving the 4 bulleted items listed on the agenda and the approval of the sealed Executive Session Minutes from the April 5, 2013 and April 10, 2013 Retirement Board meetings.

[Executive Session]

The Board thereafter convened in executive session.

[Return to Open Session]

Upon returning to open session, the Board noted for the record that the following votes had been taken in executive session:

A motion was made by Roger P. Boudreau and seconded by Frank R. Benell, Jr. to unseal the draft executive session minutes of both April 5, 2013 and April 10, 2013 Retirement Board meetings with a unanimous vote. There was a motion made by Roger P. Boudreau and seconded by William B. Finelli to approve said minutes with a unanimous vote. There was a motion made by Roger P. Boudreau and seconded by Frank R. Benell, Jr., to reseat the draft executive session minutes pursuant to R.I.G.L. §42-46-5(a)(2) as the matters affected related to pending litigation involving the Retirement Board, which was unanimously approved..

A motion was made by Richard A. Licht and seconded by John P. Maguire to remand the matter of *Albert Turcotte vs. ERSRI* to the Disability Subcommittee, and it was then unanimously

VOTED: To remand the case of *Albert Turcotte vs. ERSRI* to the Disability Subcommittee.

A motion was made by Roger P. Boudreau and seconded by John P. Maguire, it was unanimously

VOTED: To accept Charles Moreau's request to waive any entitlement to a pension benefit and to receive a return of contributions provided it is approved by the Superior Court.

A motion was then made by Daniel L. Beardsley and seconded by John P. Maguire to seal the minutes of the executive session of May 8, 2013, consistent with Rhode Island

General Laws §42-46-5(a)(2), as they contain confidential attorney client communications regarding pending and potential litigation matters affecting ERSRI. A roll call vote was taken, and the following members were present and voted Yea: General Treasurer Gina M. Raimondo; Vice Chair William B. Finelli; Gary R. Alger, Esq.; Daniel L. Beardsley; Frank R. Benell, Jr.; Roger P. Boudreau; Michael R. Boyce; M. Carl Heintzelman; John P. Maguire; John J. Meehan; Thomas A. Mullaney; Claire M. Newell and Jean Rondeau. The following voted Nay: Richard A. Licht. There being 14 votes cast, 13 voted in the affirmative, and 1 voted in the negative consistent with Rhode Island General Laws 36-8-6, Votes of the Board – *Record of Proceedings*, there being a majority vote of the members present and voting at which a quorum is present, it was then

VOTED: To seal the minutes of the executive session of May 8, 2013, consistent with Rhode Island General Laws §42-46-5(a)(2) as they involved confidential attorney client communications regarding pending and potential litigation matters affecting the Board.

On a motion made by Richard A. Licht and seconded by Frank R. Benell, Jr., to exit executive session and return to open session, it was unanimously

VOTED: To exit executive session and return to open session.

VIII. Committee Reports

Disability Subcommittee:

The Disability Subcommittee recommended the following actions on disability applications for approval by the full Board as a result of its meeting on April 5, 2013:

Name	Membership Group	Type	Action
1. Carlo Gentile	State	Accidental	Deny
2. Shelley Regan	State	Ordinary	Approve
3. Denise Monastesse	Teacher	Ordinary	Deny
4. Suzanne Marsella	Teacher	Accidental	Postpone
5. John Moniz	State	Ordinary	Approve
6. Lois DiGaetano	State	Ordinary	Approve
7. Joseph Rhodes	State	Ordinary	Approve
8. Jennifer Lambert	Teacher	Ordinary	Postpone
9. William Zambarano	Municipal	Ordinary	Approve

Name	Membership Group	Type	Action
10. Lee Brando	Municipal	Ordinary	Approve
11. Lee Fazio	Teacher	Ordinary	Approve
12. Edward Gaboriault	Municipal	Ordinary	Approve

On a motion by William B. Finelli and seconded by Michael R. Boyce, it was unanimously

VOTED: To approve the recommendation of the Disability Subcommittee meeting of Friday, May 3, 2013 on items 3, 4, 8 and 11.

John P. Maguire recused himself from the vote on numbers 3, 4, 8 and 11.

On a motion by William B. Finelli and seconded by Michael R. Boyce, it was unanimously

VOTED: To approve the recommendation of the Disability Subcommittee meeting of Friday, May 3, 2013 on items 6 and 7.

John J. Meehan recused himself from the vote on numbers 6 and 7.

On a motion by William B. Finelli and seconded by Michael R. Boyce, it was unanimously

VOTED: To approve the recommendation of the Disability Subcommittee meeting of Friday, May 3, 2013 on items 1, 2, 5, 9, 10 and 12.

Legislative Subcommittee:

Newly elected Chairman Richard A. Licht said the Legislative Subcommittee met on Monday, April 29, 2013. Members present were Frank R. Benell, Jr., Roger P. Boudreau and Attorney Mark A. Dingley. The committee reviewed a presentation presented by the Director and prepared by the system actuary Gabriel, Roeder, Smith and Company which would allow current retirees, less than age 62 and receiving Social Security Option, a one-time option to opt out of the optional form of payment. Director Licht noted that there are approximately 800 retirees currently receiving the Social Security Option that will turn age 62 after 2013. The committee discussed the logistics of the one-time option and the authority to enact such a change. After further consideration, the committee recommended that the matter be transmitted to the Rules and Regulations subcommittee for their review to determine if the one-time option could be addressed via a promulgated regulation. On a motion by Jean Rondeau and seconded by Roger P. Boudreau, it was unanimously

VOTED: To accept Chairman Licht's report and a recommendation that the matter be referred to the Rules and Regulations Subcommittee for consideration.

Procurement Subcommittee:

Treasurer Raimondo apprised the Board that there is no Procurement Subcommittee Report as the meeting was canceled and will be rescheduled by Director Karpinski.

Mr. Boudreau expressed his appreciation for Chief Investment Officer Ms. Ann Marie Fink's presentation and noted that it was very instructive. He felt it would be beneficial to implement this reporting on a quarterly basis, one month after the quarter ends, given the reporting nature of certain types of funds.

IX. Adjournment

There being no other business to come before the Board, on a motion by Frank R. Benell, Jr., and seconded by Roger P. Boudreau, the meeting adjourned at 11:12 a.m.

Respectfully submitted,

Frank J. Karpinski

Executive Director